

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

[Third Party Communication:

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:EEE:EOET:EO2

PLR-120195-19

Date:

February 07, 2020

Legend

Authority =
Commodity(ies) =
Commission =
Members =

State =
Third Parties =

Dear :

This letter responds to a ruling letter request from your authorized representatives dated August 29, 2019, and subsequent correspondence requesting a ruling that Authority's income will be excluded from gross income under § 115 of the Internal Revenue Code (hereafter "Code").

Facts and Representations

In requesting the present ruling, Authority represents the following. Authority is a nonprofit corporation organized under the not-for-profit corporation law of State. Authority was created to coordinate the operation, purchase, and sale of Commodities on behalf of its Members. Authority currently has two members: Members. The Members of Authority each own and operate facilities for the purpose of providing Commodities to consumers in their service areas. The Members buy and sell Commodities on the Commodity market. Authority represents that all current Members are political subdivisions of their respective states or entities the income of which is excluded from gross income under § 115 of the Code. All Members must be either political subdivisions or entities the income of which is excluded from gross income under § 115 of the Code.

Authority is governed by a board of directors that are elected by a majority vote of all Members. Members are required to make capital contributions to Authority and revenues and expenses flow through to Members based upon membership interest. Upon dissolution of Authority, its assets are distributed to its Members. The net revenues of Authority are distributed monthly to its Members less a reasonable retention for Authority's working capital needs. No income of Authority shall inure to the benefit of any director, officer, trustee, or private person.

Authority's purpose is to purchase Commodities on the Commodity market and resell those Commodities to its Members at a substantial savings. In addition to Commodity sales, Authority will provide Commodity management and distribution services to its Members.

Authority represents that it receives income resulting from: (1) the sales of Commodities to its Members; (2) income generated from the investment of cash from Authority's purchases and sales of Commodities; and (3) Authority's acquisition and termination of commodity swaps and other hedges related to its purchases and sales of Commodities.

In order to insure that an adequate supply of Commodities are available for Authority's Members in case of an unexpected event, and to promote cost effective participation by its Members in the wholesale Commodity market, Authority buys Commodities on the Commodity market for sale to one or more Members (or Third Parties in the balancing transactions described below). Authority also performs other services for its Members related to managing their Commodity resources. In conducting these activities, Authority performs for its Members on a consolidated basis, activities that the Members have historically performed for themselves or that would have been entered into by Authority's Members if Authority did not exist.

Authority from time-to-time generates revenues from sales to non-members. Savings or positive net margins, if any, from non-member sales are used to lower the costs of the member whose assets or contracts are involved. These sales could be accomplished by the member directly instead of through Authority. Non-member sales are generally expected to include (i) sales of Commodities; (ii) sales of Commodities with respect to supply contracts; and (iii) miscellaneous transactions, such as swap/trades, and "balancing" transactions regulated by the Commission. With respect to these sales to non-members, Authority represents that any benefit to nonmembers involved in the sales transactions is no different from the benefit that would be provided if the member itself performed the sale.

Authority represents that the Commission regulates both the transportation and transmission of Commodities. The Commission requires that transporters and market participants of Commodities be in balance—that the amount of Commodities purchased equals the amount Commodities sold. To that end, Authority's Members may use diverse methods to balance transactions of Commodities. These balancing transactions

will entail selling excess or purchasing more Commodities in an arm's length transaction to Third Parties. Authority represents that, in furtherance of maintaining its balance of Commodity purchases and sales, it expects to enter into certain transactions with Third Parties, such as buying Commodities on the Commodity market and selling Commodities to Third Parties at market rates. Sales of Commodities to Third Parties will be limited to transactions to maintain the balance of its purchases and sales of Commodity as described above and as represented to by the Authority.

Authority itself may also engage in certain transactions to hedge their Members Commodity supplies, such as entering into long-term commodity swaps to lock in the Commodity's price, and entering into commodity swaps that synthetically convert the price of the Commodity to an indexed or variable price.

Ruling Requested

Authority requests a ruling that Authority's income is excludible from gross income under § 115 of the Code because the income of Authority derives from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof.

Law and Analysis

Section 115(1) of the Code provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that income generated by an investment fund that is established by a state to hold revenues in excess of the amounts needed to meet current expenses is excludable from gross income under § 115(1) of the Code, because such investment constitutes an essential governmental function. The ruling explains that the statutory exclusion is intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of an entity engaged in the operation of a public utility or the performance of some governmental function that accrues to either a state or political subdivision of a State. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a State government and that are within the ambit of a sovereign to conduct.

Rev. Rul. 90-74, 1990-2 C.B. 34, holds that the income of an organization formed, funded, and operated by political subdivisions to pool various risks (e.g., casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under § 115(1) of the Code because the organization is performing an essential governmental function. The revenue ruling states that the income of such an

organization is excluded from gross income so long as private interests do not participate in the organization or benefit more than incidentally from the organization.

Authority is performing of an essential governmental function within the meaning of section 115 of the Code. See Rev. Rul. 90-74 and Rev. Rul. 77-261.

No private interests will participate in, or benefit from, the operation of Authority other than as providers of goods or services. The benefit to Third Parties is incidental to the public benefit. See Rev. Rul. 90-74.

Ruling

Based solely on the facts and representations submitted by Authority, we conclude that:

The income of Authority is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof, or to an entity the income of which is excluded under § 115(1). Consequently, we rule that Authority's income will be excluded from gross income under § 115(1).

The ruling contained in this letter is based upon information and representations submitted by or on behalf of Authority and accompanied by a penalty of perjury statement executed by an individual with authority to bind Authority, and upon the understanding that there will be no material changes in the facts. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination. The Associate office will revoke or modify a letter ruling and apply the revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of the transaction are materially different from the controlling facts on which the ruling was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2020-1, § 11.05.

This letter does not address the applicability of any section of the Code or Regulations to the facts submitted other than with respect to the sections specifically described. Further, except as expressly provided in this letter, no opinion is expressed or implied concerning the tax consequences of any aspects of any transaction or item of income discussed or referenced in this letter.

Because it could help resolve questions concerning federal income tax status, this letter should be kept in Authority's permanent records.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to Authority's authorized representative.

This ruling letter is directed only to Authority. According to § 6110(k)(3) of the Code, this ruling letter may not be used or cited as precedent.

A copy of this letter must be attached to any tax return to which it is relevant. Alternatively, if Authority files a return electronically, this requirement may be satisfied by attaching a statement to the return that provides the date and control number of this ruling letter.

Sincerely,

James Zelasko
Branch Chief
Office of Chief Counsel
(Employee Benefits, Exempt Organizations, and
Employment Taxes)

cc: